

References: For determination of reasonable compensation, see FTC 2d/FIN ¶ H-3706 ; United States Tax Reporter ¶ 1624.229 ; TaxDesk ¶ 276,027 ; TG ¶ 8501 .

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DEFECTIVE DONEE'S LETTER OF ACKNOWLEDGMENT BARRED CHARITABLE CONTRIBUTION DEDUCTION

Durden, TC Memo 2012-140

The Tax Court has disallowed taxpayers' charitable contribution deduction to their church because the donee organization failed to provide a properly completed contemporaneous written acknowledgment of the contribution. Although the donee twice attempted to provide letters adequately acknowledging the contribution, the letters failed to meet the substantiation requirements.

RIA observation: This Tax Court decision illustrates the need for taxpayers to be vigilant about receiving proper and timely acknowledgment of \$250 or more charitable contributions from donee organizations. A cancelled check and a simple written acknowledgment aren't enough to substantiate a deduction. Further, a failure to receive the proper acknowledgment can only be remedied by the donee within a relatively short window of time.

Background. Under Code Sec. 170, a taxpayer is allowed a charitable contribution deduction for a contribution or gift to or for the use of an organization organized and operated exclusively for charitable or educational purposes. Under Code Sec. 170(f)(8)(A), no charitable contribution deduction for any contribution of \$250 or more is allowed unless the taxpayer substantiates the contribution with a contemporaneous written acknowledgment of the contribution by the donee organization that meets certain specified requirements. Under Code Sec. 170(f)(8)(B), the donee organization must state in the acknowledgment whether the donee organization provided any goods or services in consideration, in whole or part, for the contributed property or cash. If so, the acknowledgment generally must include a description and good faith estimate of the value of any goods or services provided. (Reg. § 1.170A-13(f)(2)) Under Code Sec. 170(f)(8)(C), a written acknowledgment is contemporaneous if it's obtained by the taxpayer on or before the earlier of: (1) the date the taxpayer files the original return for the tax year of the contribution; or (2) the due date (including extensions) for filing the original return for the year. (Reg. § 1.170A-13(f)(3))

Facts. On their 2007 return, David and Veronda Durden claimed a \$25,171 deduction, mostly for charitable contributions to their church, Nevertheless Community Church (NCC), a Code Sec. 501(c)(3) organization that was eligible to receive tax-deductible contributions under Code Sec. 170(c)(2). Except for five checks totaling \$317, the checks they wrote to NCC were all for amounts larger than \$250.

On audit, IRS sent the Durdens a notice of deficiency disallowing the charitable contribution deductions.

In response, the Durdens produced records of their contributions, including copies of canceled checks and a letter from NCC dated Jan. 10, 2008, which acknowledged contributions from them during 2007 totaling \$22,517 (first acknowledgment). IRS didn't accept the first acknowledgment, informing the Durdens that it lacked a statement on whether any goods or services were provided in consideration for the contributions. The Durdens then obtained a second letter from NCC dated June 21, 2009 (second acknowledgment), that contained the same information found in the first acknowledgment, plus a statement that no goods or services were provided to them in exchange for their contributions.

Parties' arguments. The Durdens conceded that they had not strictly complied with Code Sec. 170(f)(8). However, they argued that they had substantially complied with the statute and were entitled to the claimed deductions. On the other hand, IRS contended that the first acknowledgment failed because it didn't include a statement on whether any goods or services were provided to the Durdens in consideration for their contribution. IRS also argued that the second acknowledgment, which included the statement, failed because it wasn't contemporaneous.

No deduction allowed. The Tax Court concluded that the Durdens failed, strictly or substantially, to comply with the clear substantiation requirements of Code Sec. 170(f)(8). Accordingly, their deduction for the charitable contributions at issue was disallowed.

In deciding this case, the Tax Court focused on whether the Durdens' first acknowledgment—which the parties agreed was contemporaneous—complied with the Code Sec. 170(f)(8)(B) substantiation requirements. The Court did not consider the second acknowledgment, finding that it wasn't contemporaneous.

The Tax Court noted that it had most often found substantial compliance in cases that involved procedural regulatory requirements where, despite a lack of strict compliance, the taxpayer substantially complied by fulfilling the essential statutory purpose. But the Court rejected the Durdens' contention that they fulfilled Code Sec. 170(f)(8)'s essential purpose, even though their written acknowledgment didn't include a statement on whether goods or services were provided in consideration for the contributions. The Court found, as it had in previous cases, that this specific statement was necessary for the allowance of a charitable contribution deduction.

The requirements in Code Sec. 170(f)(8) weren't only "safe harbor" requirements that didn't establish the exclusive means by which a written acknowledgment may be deemed sufficient. Code Sec. 170(f)(8)(A) clearly stated that no deduction was allowed for any contribution of \$250 or more unless the taxpayer substantiated the contribution by a contemporaneous written acknowledgment of the contribution by the donee organization that meets the requirements of Code Sec. 170(f)(8)(B). A statement on whether goods or services were provided in consideration for the contributions, as

required by Code Sec. 170(f)(8)(B), was a mandatory condition for a written acknowledgment to properly substantiate a charitable contribution.

The Court reasoned that the statement regarding whether goods or services were provided was necessary to determine the deductible amount of the contributions. It was impossible to determine from the amounts reported (or the checks produced) whether, for example, the Durdens' payments were for meals or other goods or services provided by the church. Thus, the first acknowledgment did not provide enough information to determine the deductible amount of the Durdens' contributions

The Court also did not accept the Durdens' argument that the omission of a statement regarding goods or services in the first acknowledgment was sufficient to indicate that no goods or services were provided in consideration for their contributions. The express terms of Code Sec. 170(f)(8)(B), as well as its legislative history, required an affirmative statement.

The Court further found that nothing in Code Sec. 170(f)(8) or its legislative history required IRS to look beyond the written acknowledgment when, on its face, the acknowledgment failed to provide the information required to substantiate a charitable contribution deduction.

References: For contemporaneous written acknowledgment of charitable contributions, see FTC 2d/FIN ¶ K-3933 et seq.; United States Tax Reporter ¶ 1704.50 ; TaxDesk ¶ 334,019 ; TG ¶ 19329 .

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IRS REVISES INTERNAL GUIDANCE ON RETURN PREPARER PENALTIES & UPDATES PENALTY AMOUNTS

IRS has revised the portion of the Internal Revenue Manual (IRM) dealing with preparer, promoter, and material advisor penalties. Among other things, the IRM revision expands access to pre-assessment Appeals rights under Reg. § 1.6694-4(a) (1) to also apply to other types of penalties beyond those asserted under Code Sec. 6694, and updates current penalty amounts imposed under Code Sec. 6694 and Code Sec. 6707A.

Background. IRS has penalty and injunctive authority to address improper tax return preparation and abusive transaction promoters. Preparer, promoter, and material advisor penalties are important tools for IRS to collect the proper amount of tax revenue at the least cost, notably by enhancing voluntary compliance by taxpayers.

The specific sections providing for IRS's authority include:

- Code Sec. 6694, which penalizes tax return preparers who unreasonably understate a taxpayer's liability;
- Code Sec. 6695, which penalizes tax return preparers for failing to furnish a